San Diego City Council President Pro Tem Kevin Faulconer

Fiscal Reform Agenda 2010



Presentation Summary



What are the roots of the City's fiscal crisis?

What has the City done?

What does the City still need to do?

How did the City get to this point?

- Failure to implement managed competition or pursue outsourcing
 - Voters passed Proposition C in 2006 with over 60 percent of the vote.
- Retiree healthcare
 - The City's unfunded retiree healthcare liability is currently \$1.3 billion.
- A broken pension system
 - The pension system is taking up more of the City's budget each year and will continue to do so: from \$139 million in 2004 to over \$500 million by 2025.

The root of the City's problem: A broken pension system

- The cost of pensions has gone from 7 percent of the operating budget in 2002 to 21 percent this year.
- It will be \$512 million, or 47 percent of the operating budget, in 2025 unless changes are made. (Source: IBA)
- Pension payments take up more of the City's budget each year: (Source: SDCERS)
 - 2004 \$139 million
 - 2009 \$229 million
 - 2020 \$417 million
 - 2025 \$511 million
- The City has \$2.1 billion in unfunded pension liabilities.
- How did we get to this point?

Underfunding City pensions: 1996 & 2002

- In 1996 the City was facing budget shortfalls.
- The City Manager proposed that the City balance its books by underfunding the pension system.
- The Council voted in 1996 & 2002 to pay less into the pension system than was needed to meet its future obligations.
- These proposals are known as "MP1" & "MP2."
- At the same time, the city adopted benefit increases and a new method of calculating the city's retirement costs that hid the extent of the underfunding.

From the 2006 Report of the Audit Committee of the City of San Diego, also known as the Kroll Report:

"The City's pension system was not brought to a crisis merely as a result of abnormally low investment returns. Nor was the system brought to a crisis as a result of a 'perfect storm' of unpredictable catastrophes. What brought the system to a crisis was a number of completely foreseeable financial challenges to a pension system debilitated by years of reckless and wrongful mismanagement involving any number of City and pension board officials."

The results of underfunding

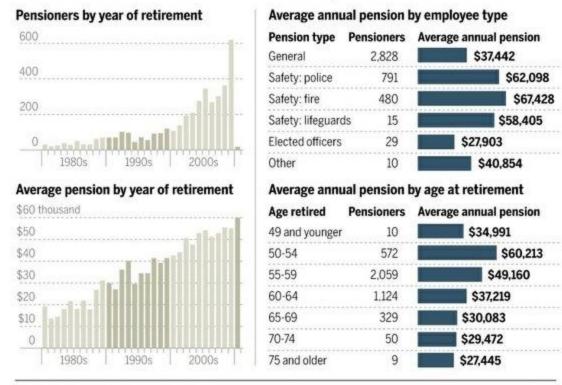
- Once discovered, those actions led rating agencies to suspend the city's credit and prevent San Diego from borrowing money at reasonable rates.
- Plans for new libraries, fire stations and infrastructure repairs were stalled, and the city wasn't able to restore its credit until 2008.

The current pension situation

The underfunding in 1996 and 2002 has enabled City workers to collect pensions 176 percent higher than they would have been previously, according to the San Diego Union-Tribune, Aug. 21.

San Diego city pensions

The average city pension is \$45,600, according to The Watchdog's analysis of data for 4,153 retirees who received checks in February. A breakdown:



Source: San Diego City Employees' Retirement System DANIELLE CERVANTES, SHAFFER GRUBB, MATT PERRY • U-T

What the City Has Done

- Created a two-tier system with smaller pensions for new general member hires effective July 1, 2009, and provided a minimal retiree health care benefit with shared funding.
- Eliminated retirement health benefits for police and firefighters who were hired after July 1, 2005.
- Eliminated SPSP (supplemental pension plan) for general member employees hired after July 1, 2009.
- Employees, including public safety, hired as of July 1, 2005 are not eligible for purchase of service credit; DROP; 13th check.
- Suspended the retiree health escalator at the FY09 level (\$740/mo=\$8,880 a year) and will be in negotiations over modification to the plan beginning on July 1, 2010.
- Implemented changes to police retirement by increasing the retirement age from 3% at 50 to 3% at 55.
- Voters passed Proposition B (passed in November 2006) which says voters must approve any increase in pension benefits.
- Voters passed Proposition C in 2006 requiring the City to implement managed competition.

What the City Still Needs to Do

Pension Reform

- Eliminate retirement offset for all elected officials, unclassified and unrepresented.
- Change age of retirement for general employees from 60 to 62.
- Establish 401k-style plan, allowing current SDCERS members to opt out and choose a 401k.
- Eliminate SPSP for lifeguards.
- Change fire from 3 percent at 50 to 3 percent at 55 and base retirement on high 3-year average instead of high 1-year average.
- Modify DROP if it's not cost-neutral.
- Eliminate terminal leave for all employees.
- Support the City Attorney's substantially equal litigation.

What the City Still Needs to Do

Retiree health care reform

- The City annually pays about 3 percent of its \$1.3 billion retiree healthcare obligation.
- Eliminating this benefit for current employees would reduce the City's obligation from \$1.3 billion to \$442 million. (Source: City of San Diego/Buck Consultants)
- Despite being eligible for MediCare, retirees and most existing employees receive retiree healthcare for life with no permanent cap on the cost to the City.

Managed Competition/Outsourcing

• If implemented, the City might not be facing budget gaps because it could save taxpayers \$80 million to \$200 million a year. (Source: Reason Foundation study)

Other

- Continuing performance audits and BPR (Business Process Re-Engineering).
- Large budget gaps recently have been closed with short- and long-term fixes, including pay reductions, layoffs and savings from a new citywide accounting system.
- The key to all of this is leverage.

Summary

- It is clear how San Diego reached this point
- Steps have been taken to address the problem
 - We know what changes need to be made
- The taxpayers expect real reform, not window dressing
 - It's time to finish the job